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TAGS: ECON EFIN EINV ETRD HK CH
SUBJECT: PRD COOPERATION BUILDING BUT LOCAL GOVERNMENTS IMPEDE SERVICE SECTOR INTEGRATION

REF: A. HONG KONG 880
¶B. GUANGZHOU 237

¶1. (SBU) Summary and Comment: Seeking to foster deeper economic integration with the Greater Pearl River Delta (GPRD), Hong Kong government (HKG) and industry leaders have built productive ties over the past several years with Mainland counterparts. Hong Kong contacts say that both sides support implementation of the Closer Economic Partnership Arrangement (CEPA), although Hong Kong industry complains that execution of CEPA at municipal levels in Guangdong could be significantly improved. Guangdong local officials' ignorance of CEPA agreements as well as their fear of potential business dislocations caused by entry into local markets by Hong Kong's world-class service providers have slowed the development of service sector integration. In the long term, Hong Kong increasingly sees its future linked to the GPRD, the world's fastest growing region. Both sides are at early stages of building business synergies and symbiotic relationships that will complement their respective strengths. Hong Kong, therefore, stands to gain much and remain relevant to the Mainland. The GPRD's rapid urbanization and rising incomes will generate significant demand for good governance, world-class service sector providers, knowledge-intensive businesses, branding, and creative industries -- areas in which Hong Kong excels. The pace and scope of success, however, will greatly depend on education, information sharing, and smooth implementation at the local level. End Summary and Comment.

Hong Kong's Major Role in Explosive GPRD Growth
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¶3. (U) The Greater Pearl River Delta (GPRD) includes Hong Kong, Macau and the Pearl River Delta Economic Zone (PRDEZ) made up of Guangzhou, Shenzhen, Dongguan, Foshan, Zhongshan, Zhuhai, Jiangmen and parts of Huizhou and Zhaoqing. It continues to be one of the most economically dynamic regions in the world since the launch of China's reform program in
¶1979. The PRDEZ owes its success largely to its proximity to Hong Kong, which has provided capital, management, technology, market knowledge, and access to international markets. According to the HKG's InvestHK Department, Hong Kong has been the source of approximately two-thirds of the cumulative FDI into the PRDEZ since 1979. These contributions from Hong Kong played a major role in the PRDEZ's boom, while supporting Hong Kong's development into a management, coordination, information, business service, logistics and financial center of global importance. The PRDEZ's GDP grew from just over USD8 billion in 1980 to more than USD89 billion in 2000 and USD269 billion in 2006. During those 26 years, the average real rate of GDP growth in the PRDEZ was 16.3 percent, compared with 9.8 percent for the PRC as a whole. Although the PRDEZ contains only 3.5 percent of the PRC's population, in 2006 it accounted for 18.8

percent of foreign direct investment and 28.8 percent of total trade (latest statistics available).

CEPA and Transportation Infrastructure

¶4. (U) The Closer Economic Partnership (CEPA) was signed in 2003 by the PRC and HKG and came into effect on January 1,
¶2004. Under CEPA, zero-tariff treatment has been extended to most products, and preferential access to the Chinese Mainland was granted across a broad spectrum of service sectors. Annual supplemental agreements extend these priveleges even further. To facilitate further economic cooperation and integration, with an eye toward developing concrete measures to incorporate into the PRC's next Five Year Plan, senior HKG and Guangdong officials in August 2009 participated in the latest annual Hong Kong-Guangdong Cooperation Joint Conference. They reiterated their full support of the sixth annual supplement to CEPA that will take effect on October 1 (ref A). They also pledged to rapidly complete planned construction of multi-billion dollar cross-border infrastructure projects. These include the Hong Kong-Macau-Zhuhai bridge and the Guangzhou-Shenzhen-Hong Kong Express Rail Link.

HK, PRC and Guangdong Officials Support Integration Goals

¶5. (SBU) HKG Trade and Industry Department (TID) Principal Trade Officer Doris Chan told Econoff on September 4 that HKG and PRC economic integration efforts are guided by The Outline of the Plan for the Reform and Development (OPRD) of

the Pearl River Delta for 2008-2020, published by the PRC's National Development and Reform Commission (NDRC) in December 2008 (ref B). Chan said TID meets with PRC Ministry of Commerce officials 3-4 times per year on policy issues related to economic integration, while maintaining a "very good" working relationship with Guangdong officials. "They are as serious as we are about pursuing economic liberalization," she said. Government-to-government, business, academic, and interpersonal exchanges between Hong Kong and PRDEZ cities continue to grow. Visa restrictions for PRDEZ residents visiting Hong Kong have never been looser, record numbers of Mainland students (7,712 as of September 2008) study in Hong Kong, and strong statements from Guangdong's leadership in recent years have called for greater cooperation with Hong Kong and Macau.

¶6. (SBU) Asked whether she had any criticism of Guangdong's dealings with the HKG on economic integration issues, Chan responded that they needed to enact new regulations at a faster pace to meet the timing expectations of Beijing and Hong Kong. Chan also stated city officials in Guangdong sometimes either ignored agreements reached at the national and provincial levels with the HKG or were simply not aware of them. "Provincial and local rules, regulations and procedures are not necessarily synchronized and sometimes the message from senior Guangdong officials isn't delivered to city officials in an accurate and timely manner," she said. Chan suggested that more training of local level officials was needed in Guangdong, especially with regard to specific CEPA-related agreements and obligations.

"Gate is Open, But Door is Shut"

¶7. (SBU) The Chairman of Hong Kong think tank Bauhinia Foundation Research Centre, Anthony Wu, told Econoff on September 9 that Guangdong's "bureaucracy and fiefdoms, especially at the local level," impeded progress toward economic integration with Hong Kong. "The big gate is open, but the small door is shut," he said, citing a local proverb. Trade and Development Council (TDC) Chief Economist Edward Leung told Econoff on September 14 that local business

interests in Guangdong felt threatened by the incursion of "Hong Kong pros" into their respective markets. He cited the difficulties faced by Hong Kong investors in setting up wholly-owned outpatient clinics in Guangdong, as allowed by Supplement V to CEPA. "They face local resistance such as anti-competitive zoning restrictions and rules, and city officials typically don't process the necessary paperwork in a timely manner," he said.

HK Cooperates with China to Court Investment

¶8. (U) InvestHK is the HKG entity tasked with promoting and facilitating foreign direct investment in Hong Kong. InvestHK uses its four Mainland branch offices (in Beijing, Guangzhou, Shanghai and Chengdu) to field Hong Kong investment inquiries from Mainland companies, liaise with provincial and local officials, and arrange joint participation in FDI promotion events. To support their joint FDI marketing trips abroad, InvestHK and Guangdong officials often invite banks, accounting firms and multinational corporate professionals to share their companies' positive GPRD operating experiences with potential investors. She said, "They're good at providing concrete examples of how the strengths of Hong Kong and Guangdong complement each other."

Mainland Investment in HK Accelerating

¶9. (U) Mainland companies increasingly invest in Hong Kong. InvestHK Associate Director General Victoria Tang told Econoff on September 16 that investment inquiries from Mainland China-based companies account for approximately 15 percent of her group's workload. Tang said, "We support China's 'Going Out Policy' by encouraging Mainland companies to operate first in Hong Kong for 3-5 years, before they venture out into foreign markets. Here they establish international contacts, gain experience and build the confidence necessary to operate in a different environment." She said 250 Mainland companies commenced "significant" operations in Hong Kong since 2002, including several law firms, with the investment pace accelerating in the past couple years. Tang also noted Mainland companies comprise almost 25 percent of the 1,109 names listed on the Hong Kong

Stock Exchange (HKSE) and just under half of the HKSE's total market capitalization.
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